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THE DEVELOPMENT OF BANKING

C. M. Short

"BANKING, more than any other business, is vested with a large trust in behalf of the public, and the functions that it performs in the modern economy with its high degree of interdependence are of vital concern to every citizen. . . .

"The public interest has been recognized, also, because the primary function of banks is to mobilize these liquid capital resources; to keep them constantly at the disposal of agriculture, commerce, and industry; to guide them, after credit analysis, into the most profitable uses compatible with safety; to maintain them for return to owners on demand or after notice; and to make available and serviceable additional bank credit funds based upon them. Furthermore, the public interest has been recognized because the mechanical function of banks is to provide the machinery for cheque payments, by means of which the available liquid capital resources are efficiently and economically transferred from one individual or concern to another in business transactions."

The foregoing quotation is from a book, *"The Banking Situation in the United States,"* prepared and published a few years ago by a large economic research bureau, the National Industrial Conference Board of New York. Apart from stressing the obvious fact that banking is of great public interest, this statement emphasizes the ideal of banking practice, the mobilization of capital into channels where it may become fluid and be used over and over again for the public good.

While much of the monetary development of ancient times is shrouded in the mists of antiquity, we know of course that there were money-lenders and money-changers as soon as, or shortly after, the system of barter (the exchange of goods in kind) commenced to wane and metallic money came into existence thousands of years ago as a means of exchanging goods. Then, as a convenience in trade transactions—to express a consideration on paper—and as a protection against robbers, the destructive elements of nature and oppressive rulers, always on the search for money with which to finance their wars, the first real instrument of credit, the bill of exchange, was

devised. By 1148 A. D. the Republic of Genoa had an institution of private ownership for the purpose of lending money to the State and for insuring the payment of interest on such advances as well as for the return of the principal by the collection of certain taxes. The true prototypes of our present-day banks were, however, created some time late in the 13th century when a number of institutions were established in Venice, probably first as an adjunct of the foreign money dealers, with a business resembling that which banks now transact, the accepting of deposits and the discounting of bills representing trade transactions. Early in the 15th century payments by transfers on these Venetian banks' books were recorded, a practice which may be regarded as the forerunner of the modern method of making payments by cheques on banks. That banking was even then recognized as an important segment of the economic system may be seen by the fact that while private banking was suspended by a decree of the Venetian State late in the 16th century, after but a few of the hundred or more of established banks had survived the vicissitudes of the troublous times, a government-owned institution was formed (probably the first of the national or, as we now call them, central banks) because it was felt that Venice could not exist without banking facilities.

Holland was the scene of the next important development in banking. That country had assumed a leading place in world commerce by the 16th century and in 1609 an exchange bank, later known as the Bank of Amsterdam, was established which for over two hundred years was one of the most influential institutions of its kind. It fell into difficulties as a result of large loans to the Dutch East India Company and the City of Amsterdam and was forced to close in 1820. This bank served as a model for the formation of similar institutions, notably in Hambourg (which was becoming an important commercial centre) in 1619, and in Rotterdam in 1635.

Thus we find that modern banking had its genesis in Continental Europe. Historians refuse to recognize the existence of banking, in the true sense of the word, in England until the 17th Century. There were money organizations of primitive character following the introduction of metallic money for general use into the country, shortly after the Norman Conquest; thus, "The Brotherhood of St. Thomas-a-Beckett of Canterbury" formed in 1248 is recorded as having been of great service to the crown in advancing money by way of loan. There were money-lenders, who accommodated the English nobility at high

interest rates in return for security over the borrowers' property. And from the time of James I a group of people known as goldsmiths had issued their receipts for coin deposited with them who in time realized that, as the possibility of simultaneous demand for the encashment of all outstanding receipts was remote, and therefore that full metallic cover was unnecessary, a fair reserve might be maintained against immediate withdrawal and the balance lent at interest. But it was about 1650 before the movement for a real banking system in England began to take definite shape. With the example of Continental Europe's credit facilities and the influence of these upon commerce before them and following a lengthy period of dishonest monetary practices both by certain goldsmiths and by rulers, notably Charles I and II, as well as of a mounting public debt incurred largely through wars, numerous public-spirited citizens advocated the establishment of some kind of a real bank. This movement was finalized in 1694 with the founding of the Bank of England. The primary purpose of this institution was to relieve the Government of a serious debt problem, which it surmounted by providing a loan of £1,200,000 in about ten days' time, obtaining therefor the privileges of issuing its notes for public circulation and of being the only corporate banking institution until 1833, when the private banks, some the outgrowth of the better class of goldsmiths, were permitted to form into joint stock organizations, from which the great commercial banks of the present day have sprung.

Before we turn to the historic perspective of the Canadian banking system and the manner in which it operates, I should explain that as a result of experience in the lengthy period in which banking has been in the process of formation the world over various types of banking have evolved. In broad division, banks are classified as:

1. Central Banks.
2. Intermediate Credit Banks.
3. Mortgage Banks.
4. Commercial Banks.

There is another type of banking, the issuance of, and the trading in, securities, but though it is a highly important service in finance it is generally regarded as distinct and separate from banking proper. Taking the enumerated types of banking, it may briefly be explained that the function of a central bank is to exercise control, by various methods, over the supply of credit and currency of a country, as well as over its foreign exchanges; intermediate credit and mortgage banks

are for the provision of credit, mostly to individuals, for long or fairly long terms, say, from one to twenty years, usually on the security of equipment or land; while commercial banking is the furnishing of short-term credit for financing the production and distribution of consumption goods, the relative loans being, as a rule, self-liquidating. If it were generally understood that the last-mentioned type of banking is *not the provision of capital,* but the transference of capital into liquid form through production and trade we should be spared most, if not all, of the conflicting opinions on banking which frequently meet the eye these days.

The Canadian banking system has developed in accordance with the financial and commercial requirements of the country. The first Canadian bank was founded in 1817, primarily to ensure a reliable currency for, in common with other parts of the New World, Canada had passed through a long period of unstable and uncertain currency. In the days of the French Regime, up to 1763, government obligation tokens known as "ordonnances" and "card" money, made from playing cards, had served as currency, but in the absence of metallic cover, these were really forms of "fiat" money and ultimately depreciated in value. After the British occupation in 1763, the common metallic currency of the New World, the Spanish dollar, was in general use, but the lack of sufficient coins still hampered trade. Several attempts were made to secure bank charters, on the establishment of representative government by Parliament in 1791, but as these attempts were unsuccessful the inconvenience persisted. During the war of 1812-15 a temporary expedient was found in the issue of Army Bills but on their redemption and removal from circulation in 1817 it became clear that the establishment of banks of issue could no longer be delayed. Between 1817 and 1825 banks were established in four Canadian Provinces under Provincial charter. Although specie payments by the banks were suspended during the rebellion of 1837, not one Canadian bank failed between 1829 and 1866. When the Provinces of Canada were confederated into the Dominion of Canada, banking legislation passed into the domain of the Dominion. The existing banks, therefore, came under the new jurisdiction and the first general Bank Act was passed in 1871. By this Act the charters of the banks were renewed for ten years, and there thus arose the practice of a periodic revision of the Act, which with two unimportant exceptions has since taken place every decade.

The last general revision occurred in 1934. Such, in brief, is the historical background of the Canadian banking system.

Canadian banks are commercial banks in the strict sense of the term, for one reason, because Canada, still far short of economic maturity, has no great accumulation of reserve wealth, but must keep most of her comparatively small capital resources mobile and so available for use over and over again in a short space of time.

In the presence of facts which have recently become quite well known, it is fortunate that the principles of short-term commercial banking have been followed by the chartered banks in Canada. Participation by the commercial banks of this country in large-scale industrial banking, such as occurred in certain European countries, would have increased considerably the narrow field of banking profit. But our institutions had before them not only the need to keep the bulk of Canada's capital resources fluid (and thereby available at all times to all classes of people as their activities turned each year first to production, then to distribution and finally to sales), but also the necessity for avoiding, in the interests both of depositors and borrowers, a condition such as that described in "Commercial Banks," a work of the Economic Intelligence Service of the League of Nations: "The risks involved in *immobilising* a large proportion of short-term funds in long-term credits became very patent during the difficult periods of shaken confidence through which most countries passed after the war." The avoidance by Canadian banks of this long-term credit risk, which greatly accentuates the forces of depression, has been a stabilizing factor for which there is every reason to be thankful.

Now as to the performance of Canadian banks. As you know, these institutions have undergone the most searching analysis, first from the Canadian Macmillan Committee (The Royal Commission on Banking and Currency), and later by the Parliamentary Banking Commission which undertook the decennial revision of the Bank Act in 1934. In each instance the verdict was that the operations of our banks were satisfactory. Indeed, an eminent British banker, Sir Charles Addis, who served as a member of the Macmillan Commission, made this statement in response to the banks' brief:

"You have been subjected to a searching questionnaire and you have given us a straight reply. You have refuted many ill-founded and, I may add, in some cases, malicious charges which have been levelled at the banks. You have done so with a dignity, with a moderation

and with a frank sincerity that compel conviction. I believe that your document will stand as an historical defence of the Canadian banking system. If this Commission should do nothing more than to elicit this response it would not, in my judgment, altogether have failed in the task allotted to it."

I should like the readers of this Journal to go further with me to determine, from official and other authoritative records, whether the Canadian banking system has functioned in the public interest. It is a matter of record that there has been no loss in the Canadian bank note issue in a period of over fifty years; in other words, the acid test of complete redemption at face value has been met, a noteworthy record when it is considered that the public of other countries sustained heavy losses from currency holdings. It is also a matter of record that there has not been a bank failure in Canada since 1923, when one of the small institutions closed, with deposit losses, however, which were localized. This failure, it might be noted, was the first since 1914. The bulk of the public savings, bank deposits, were protected during the Great Depression from the almost world-wide depreciation of values. But the whole story in this respect is not in such a bare recital of deposit protection. Bank deposits serve as the bulk of a country's working capital and are therefore available for loans (after a certain proportion is set aside for necessary reserves) to farmers, manufacturers, millers, mining companies, forestry industries and merchants, which in turn breed a certain amount of new deposits; money, it may be noted, feeds upon itself. They serve also as a reservoir of purchasing power, not only tiding over a difficult period those owners whose incomes decline or cease entirely, but also supplying funds for investment in capital goods as national confidence is restored and the savings public decides to replace some of its equipment. The effective operation of this latter factor has been demonstrated in recent years as these funds were used more actively for the purchase of goods such as automobiles and certain house-furnishings, the greater demand being reflected, of course, in employment conditions. The availability and effective use of bank deposits in Canada in themselves proved to be powerful economic restoratives.

There is another stage of Canadian banking to be depicted, namely, the lending record. Controversy has arisen from time to time over the question of whether Canadian banking fulfilled its function of meeting the credit requirements of the country. Frequently statements

have appeared that the banks denied the public sufficient credit in the pre-depression period to sustain business activity on the high level of that era; that contraction of bank credit not only caused the depression, or at least contributed greatly to it, but also precipitated the severe decline in commodity prices which unbalanced the relationships between creditors and debtors; that it is now impossible for people to borrow money from their bankers; and finally, that poverty and distress persist in many households because banks will not make more money available to the populace. These are serious charges, which if capable of substantiation would justify the salutary measures for bankers advocated in certain circles. But as they rest upon hastily considered opinions without reference to easily accessible records they are incapable of proof. True, one author will point to the marked fall in bank commercial loans (advances to the business community), while another will cite an instance of some worthy farmer being refused accommodation by a branch bank Manager. In the one case two simple factors are ignored, namely, that commercial loans are but part of total bank credit and that the height of these transactions is governed in considerable degree by the commodity price level. In the other case it will be overlooked that a depression reduces the number of credit-worthy people, or that one banker's over-cautiousness in difficult times is not representative of the general policy of his institution; those who are familiar with bankers know that they reflect the qualifications and frailties of the human race about as closely as any other class, and that apart from their proneness to mistakes in individual transactions, they include both extra free, as well as extra careful, lenders, the policy of one group probably acting as an antidote to that of the other. So the question of whether there has been sufficient bank credit cannot be settled merely by discussing one section of the credit structure, or by stressing the inability of some individuals to obtain loans.

Fortunately, the question before us can be settled by something better than generalities. We can turn to public records issued by the Dominion Government, those showing the course of business activity, the movement of commodity prices and the consolidated position of the banks. Total bank credit in Canada is made up of current loans and advances to the Canadian business community, loans to governments and municipalities and investments, mainly in government security issues; these investments are included because the increase of recent years is represented for the most part by new issues, the resultant funds

being used to maintain public services and unemployment relief and thus contributing to the national income as much as did loans to private enterprise. In other words, bank absorption of government securities is in reality the lending of money to governmental bodies who turn the proceeds over to the public just as the business community does when it is accorded commercial loans.

A glance at the consolidated Bank Statement issued monthly by the Dominion Government will show that the course of bank credit was similar to that of business activity until 1929, when a sluggish export movement of both new and old wheat, together with a sharp mid-year rise in wheat prices and a rapid delivery of the new crop by the growers to country elevators, caused a marked up-turn. One noteworthy feature of the Government's report is that business activity declined sharply in 1929 (as did wholesale prices) *prior to the downturn of bank credit.* One of the most arresting features, however, is that the volume of bank credit as a whole, as well as of commercial loans, was consistently above the level of business activity.

A few words as to the downward trend of commercial loans after 1929. One Dominion Government return, *Prices and Price Indexes,* shows the commodity price level to have been 25 per cent lower than in 1929. It required, therefore, just 25 per cent less money for the financing of business than in 1929. This, then, explains much of the decline in bank commercial loans. The explanation of the decline not represented by the fall in commodity prices lies mainly in the desire of strong business concerns to keep out of debt in a period of waning confidence and to accumulate funds with which to finance future operations, as well as (during the early period of business revival) in a tapping of large accumulated stocks of raw materials for industrial production and, particularly, the financing of a greater volume of exports by letters of credit established by foreign purchasers of Canadian products for which the domestic banking facilities were partly employed. We have, however, seen commercial loans rise quite markedly in the last few years, even during the recent economic recession.

The actual scene, therefore, as drawn from official records, is that there has been sufficient credit, if not more than sufficient, to support the country's economic structure, while the downturn of that section of bank credit, commercial loans, is largely explained by the fall in commodity prices. If one wishes to quarrel with this summary, one must dispute the records of the Dominion Government.

What Canadian banks have done to support the country during a depression of unparalleled scope and intensity by guarding the public savings and by keeping credit channels open need not be regarded as more than the fulfilment of a public trusteeship vested in them. These institutions, then, should not claim to have done more than their duty. But the performance of that duty warrants recognition.

AN HISTORIC STUDY OF THE DEVELOPMENT OF COMPANY LAW AND PROCEDURE

By C. E. WALKER.

THE history of the development of the various forms of mercantile and manufacturing organizations is an interesting study. Even before the Norman conquest mercantile guilds were established in England. These guilds were given the right of perpetual succession in property. The deed authorizing one of these guilds states that it was formed "to abyde, endure and be mayntayned without end." Another was founded "evermore to lasten."

Early in the development of the different forms of business organization a spirit of exclusiveness was fostered and in many cases candidates for admission had to swear not to betray their affairs, from which practice there emerged the monopolistic idea in certain of the trading guilds.

In contrast with the general partnership in which each general partner was a general agent of the firm, the government of the early guilds was committed to a board of management. In the Guild of the Holy Trinity, organized at Lancaster toward the end of the 14th century, the governing body consisted of "twelve good and discreet men." Later, in 1505, a charter was granted to The Fellowship of the Merchant Adventurers of England, which provided for the election of a governor and "four and twenty of the most sadd, discreet and honest persons" to be called assistants to the governor.

The forerunners of the first joint stock companies were large partnerships formed for working the tin mines of Cornwall. In the reign of Edward VI (1547-53) such a partnership was formed for the smelting of iron, and soon after, the development of the textile industry created an increased demand for capital. The partnership form of organization and method of raising capital proved unsatisfactory, however, and the joint stock idea was gradually introduced. The first English joint stock company was the Russia Company formed in 1563, and in the same year another joint stock enterprise was formed to

trade with Africa. Sebastian Cabot, who had a knowledge of the joint stock system which had appeared a little earlier in Italy, was one of the founders of the Russia Company. This company was formed "with one common stock" and members were prohibited from trading on their own account. A capital of £3000 was subscribed by calls of £25 per share. Some of the first trading companies returned the capital in full or in part at the conclusion of each voyage or venture and obtained new subscriptions of capital for later ventures.

The practice of the transferring of shares was introduced in 1568 when a charter was granted incorporating the Mineral and Battery Works, so as "to prevent the great inconvenience which might otherwise result, on the death of one of the then existing partners." Finding themselves short of capital, they divided their undertaking into twenty-four shares, half of which were sold in England and half in Germany. The discovery of gold, copper, and silver soon after the company's incorporation raised expectations of large profits and premiums as high as £1200 were paid for shares in the company. The price of shares became so high that it became difficult to sell them, so in 1571 shares were first subdivided and sold in halves, quarters and eighths. Management was by a board of directors elected by the shareholders at their general meetings. This company leased certain of its properties to three of its shareholders at a rental of £150 per year. One of the three shareholders, Sir Richard Martyn succeeded in purchasing shares in the business until he held a controlling interest. He then used his voting power to reduce the rental to £40 per year.

It was a recognized practice followed by the various industrial companies that dividends be paid only out of profits in order that the capital fund should be kept intact. In some cases, however, as previously indicated, the capital and profits were distributed in full to the shareholders at the conclusion of a voyage or venture.

The par value share was first issued by the East India Company, shares having a par value of £400 each, being issued in 1613, payable in four equal annual instalments. The practice of offering shares for public subscription was introduced by this company in 1615, when the directors of the company ordered that certain shares should be auctioned to the public "whereby they may better know the worth of their adventurers which will give a good reputation to the voyage if the stock shall be sold."

In 1620 rules were first made to determine the relation of votes to shares. The East India Company decided matters by show of hands. However, the Mines Royal Company, which had some years before subdivided its shares into halves, quarters and eighths, introduced the idea of voting according to the shares held by its members. The resolution passed was as follows: "the voice of everyone having a quarter part is to be held of as great account as the voices of two others, having but half-quarter parts apiece, to be esteemed as so many persons having but a half-quarter apiece." They required a quorum of twelve shareholders.

The limitation of the liability of shareholders was first attempted in 1634. The Fishery Society, a subsidiary of the East India Company, had suffered heavy losses during 1633 and 1634 and it found difficulty in obtaining the new capital necessary to finance its ventures. It therefore passed a by-law declaring that shareholders subscribing additional capital should be "exempt from any liability for this deficit." No further attempts to limit the liability of shareholders seem to have been made until 1662 when an Act of Parliament was passed enacting "that Subscribers to the East India, Africa and Fishery Companies should not pro tanto be subject to the law of bankruptcy in the event of losses being incurred by any one of the Companies named." This reduced the liability of the shareholders to the amount unpaid on their shares, a distinct advantage over the shareholders of unincorporated companies.

Up to this time, shareholders seem to have enjoyed the privilege of access to the books of the company. A controversy arose between the shareholders of a subsidiary of the East India Company and the company, and a motion was made for the appointment of a committee of inspection. The governor, however, refused to put the motion to the meeting or to record it in the minutes. It was found that because of the factious nature of the opposition, shareholders had copied accounts and documents and made ill-use of them by divulging secrets of the company. It was therefore resolved that in future no shareholder should be permitted to have access to the accounts or to read any document without the consent of the committees or board.

As previously indicated, the terms under which capital was subscribed varied with different companies. Capital in the East India Company for each voyage was distinct, although in some cases the capitals subscribed for different voyages were merged. In 1603, a new

method was adopted by which subscriptions extended over four years and in 1617 "the Second Joint Stock was to last for eight years." Companies formed to develop industries, however, had permanent capital from the first. Later the capital of the trading companies also was made permanent. New capital subscribed by shareholders of the East India Company in 1658 had been adventured for seven years only and this capital should have been returned in 1665. The balance sheet in 1664 showed net assets equal to 130% of the capital subscribed and in August, 1665, a dividend of 40% was declared. In spite of this dividend the stock sold at only 70% of the amount paid. Had the assets been distributed and the stock wound up, it would have been difficult if not impossible to secure new capital, so the Court decided that the stock should be made permanent.

The prospectus seems to have made its appearance first in 1681. At that time a cloth manufacturing company was founded at New Mills in Haddingtonshire. At its formation a memorial or prospectus was circulated which announced a capitalization of £5,000 and elaborate calculations were submitted to show how a profit of 25% on the capital, each year, was anticipated. This company was somewhat unusual insofar as its organization and methods of operation were concerned. None but "actual trading merchants" were accepted as shareholders. Costs of cloth were determined and profit added to yield income on the capital of the company. Bales of cloth were then distributed among the members by lot and charged at the prices determined as indicated above. The shareholders were really a regulated company as retailers and a joint stock company as manufacturers. In spite of the high hopes of the incorporators as to profits, their by-laws provided that no dividend was to be paid for three years and then only five per cent for three years.

In 1682 the East India Company doubled its capital by profitable trading. The nominal capital consisted of stock on which only 50% had been paid up. The company had built up a large reserve fund out of profits. Instead of distributing the profits to the shareholders in the form of a cash dividend, they were authorized by the Court to extinguish the liability for the 50% unpaid on the shares and thus virtually declare a 100% stock dividend or bonus to the shareholders.

During the latter part of the 17th century, the growth of industry became quite marked and the number of companies incorporated greatly increased. In 1692, John Houghton began to publish a financial paper

stressing in particular the industrial progress of the time and also listing the current quotations of the shares of the various joint stock companies. By 1695 the shares of no less than one hundred and thirty-seven companies were included in the published lists. In addition to the activities already referred to, companies at that time were engaged in such undertakings as sawmills, stage-coach lines and industries manufacturing whalebone whips, leather goods, powder, glass, paper, broadcloth, wool-cards, sailcloth, ropes, cordage, sugar, rum, soap, etc. The shares of these companies were in most cases of a nominal value, and of smaller amounts than those of the earlier companies.

The practice of accepting payment in instalments existed from the time of the earliest issues of shares. In many cases, however, shareholders were dilatory and paid the instalments only under pressure. It soon became apparent that some more effective means must be taken of dealing with such delinquent subscribers and in 1690 the Sword Blade Company incorporated in its charter a clause which authorized the company to require the forfeiture of shares on which calls were in arrears.

In the period from 1690 - 1695 stock exchange dealings were first developed. Time bargains were made, options were purchased and the fluctuations in prices were quite as marked as today. Brokers' fees were fixed at 5s per share. In 1691 an English Linen Company put out an issue of shares at £50 per share. In 1692 the high and low of these shares were £42 and £29 respectively. The practice of issuing bonus shares had been introduced and resulted in investors anticipating the practice and bidding heavily for shares of companies likely to follow the practice.

The optimistic attitude of investors and speculators opened the way for exploitation by unscrupulous promoters. A company incorporated as The Mine Adventurers Company had been quite successful and its shares were popular on the market. In 1698, Sir Humphrey Mackworth formed a syndicate which proposed to purchase the interest of existing shareholders on behalf of a new company. The existing shareholders were offered £20 cash for their shares or the privilege of converting them into bonds (so-called) of the new undertaking. Additional bonds were issued to the public, the purchasers acquiring rights to bonus shares in the new company. The holders of the bonds were entitled to a fixed dividend of 6% and to repayment of the principal while the holders of shares were entitled to the remaining profits. The

effect of this arrangement was greatly to distort the capital fund of the company. A charter was granted to the syndicate and the new company held the confidence of the public until 1707 when signs of mismanagement became apparent. To aid in its financing, the company organized a department or branch to conduct a banking business, but to finance this expansion a new issue of shares was necessary. This new venture proved a failure and the creditors of the bank pressed urgently for their money, and accusations of fraudulent management became general. They applied to Parliament for redress, and an inquiry was ordered. In 1711, an Act was passed declaring all shares other than the original as illegal, and the holders of the illegal shares were declared creditors of the company.

In spite of the disclosure of such exploitations as the one described above, the public confidence in the joint stock company continued. In the period from 1700 - 1720, great numbers of new companies were formed and by 1720 the capital of such companies in England reached an aggregate of £40,000,000 which represented approximately one-eighth of the entire national wealth. The climax was reached in the frenzied financing of the South Sea Company which at the time of its collapse possessed control of the greater part of the trading wealth of the country. The results of this financial crash are known to some extent by all readers of history and need not here be repeated.

The joint stock company naturally came to be regarded with strong disfavour, and soon The Bubble Act was passed declaring such companies to be common nuisances and indictable as such.

Although this Act was not formally repealed until 1825, it had in the meantime proved ineffectual in the checking of the growth of joint stock companies. The government found that such companies had to be tolerated and resorted to the wiser course of attempting to regulate what it had been unable to control.

One of the great evils of this type of company arose from the fact that it was unincorporated. Such companies were formed of large groups of individuals, and a person dealing with them did not know with whom he was contracting or against whom he might take legal action. By an Act of Parliament passed in 1833, the Crown was empowered to grant to such companies letters patent by which they became legal entities which could sue and be sued in the name of the company. The shareholders continued to be liable, however, for the debts of the com-

pany when the company's assets were not adequate to meet the payment thereof. For this reason, the public was naturally reluctant about investing its savings in any enterprise where such risks attached to unlimited liability. The natural growth and expansion of trade and industry were naturally retarded by the lack of capital. The need of limiting the liability of the shareholders to the amount of their investment became urgent and was finally recognized by Parliament as an economic necessity. By The Companies Act of 1862, all associations of more than twenty persons were prohibited from carrying on business without registering under that Act and all shareholders of such companies were granted limited liability. Thus, at this date begins the history of the limited liability company.

The privileges and advantages which are afforded to the shareholders of the limited liability company should naturally be accompanied by proper safeguards to the public.

It is interesting to note the attempts which legislators have made to provide adequate safeguards as shown in the present legislation applicable to limited liability companies.

The obligation to create a capital fund and keep it intact is an essential offset to the privilege of limited liability. Prior to 1862 the shareholder of the joint stock company was liable for the company's debts, the same as the general partner of a firm still is, for the debts of the firm, that is, to the full extent of his private property. The creditors of a limited liability company, however, can enforce their claims only against the assets of the company, hence the necessity that the capital fund be kept intact in their interest.

It has been implied from the inception of the joint stock company that the "capital" of the company represented the aggregate of the cash investments of the shareholders of the company. Unscrupulous promoters, however, from time to time have issued shares for which cash or a fair cash equivalent was not received by the company. The courts have not assumed the responsibility of determining the adequacy of the consideration received by companies for shares issued, that is, they have never acted as an appraiser of properties, services or rights given in consideration of shares issued.

The attitude of the courts is best shown, possibly, in the decision in the English case of the Eddystone Marine Insurance Company Limited, which case is recognized as the leading authority in the matter. The liquidator of the company after his appointment examined the share

register and discovered that the company was registered in the year 1887 with authorized capital of £20,000 of which £4,000 was issued in shares fully paid. A year later, the directors of the company decided that a further issue of £6,000 in fully paid shares should be allotted to the existing shareholders in consideration of services rendered to the company. At a special meeting of the shareholders the following resolution was adopted: "That in consideration of the services rendered to the Eddystone Marine Insurance Company Limited in its formation and in establishing its business by (the shareholders of the company) it is hereby resolved that 300 shares at £20 each in the said company be credited in the company's books as fully paid up, free from any liability respect to the shares issued to them as fully paid.

The shareholders approached the Court and asked that their names be removed from the list of contributories, but the judge gave a decision against the shareholders. The judgment was appealed but the Court of Appeal unanimously upheld it.

In the course of examination, one of the directors said that the shareholders thought they had built up a "little gold mine" and that when they decided to invite the public to subscribe capital they thought it was only right that the shareholders who had commenced the company should get some benefit in addition to the shares originally applied for by them.

The presiding judge, in summing up the case, said: "Now if that is so, I think that these shares never were paid for. As I understand the law, shares cannot be paid for except *by money or money's* for such payment, and allotted to the said persons in the following proportions," etc.

An agreement was then entered into between the company and its shareholders which set out that the company was indebted to its shareholders for services rendered relative to the formation of the company and in establishing its business and that the company wished to remunerate such shareholders by the issue to them of 300 shares of £20 each fully paid.

The shares were thereupon issued to the directors and shareholders equally.

The business did not prove profitable and two years later the Court was asked to wind up the company.

The liquidator, discovering the facts as indicated above, placed the names of the original shareholders on the list of contributories in

worth . . . and shares cannot be paid for by treating as a debt that which was not a debt at all—there never was a debt due to them from the company for those services—that being so, it appears to me plain that there was never anything that the law could treat as payment for those bonus shares."

It is of interest to note that the Court applied this ruling at a time when there was in fact no specific provision to that effect in the Act. The section 96 B(1) of The Dominion Companies Act now in force however provides: "The directors of a public company shall not authorize the issue and allotment as fully paid of shares in the capital stock of the company having a nominal or par value, except for a consideration payable in cash to the total nominal amount of the shares so issued or for such consideration payable in property or services as the directors may determine by express resolution to be in all circumstances of the transaction the fair equivalent of cash to the total nominal amount of the shares to be issued."

While the provision applies to "shares having a nominal or par value," the courts would no doubt apply the same principle to "the issue and allotment of shares without nominal or par value—for such consideration as may be fixed by the board of directors of the company." It is apparent that a uniform practice should be observed in determining the adequacy of the consideration received for any and every issue of shares.

The Court has also established a further effective safeguard by ruling that "a promoter of a company, though not a director, who nominates directors who perform under his influence and control stands in a fiduciary relationship to the company and is bound to make full disclosure of all material facts concerning his personal interest in company dealings and transactions." In the recent case of Proprietary Mines Ltd. v. McKay, Ontario Supreme Court 1938, the promoter had obtained shares as secret profits in the sale of certain mining claims to the company and had disposed of shares illegally against the best interests of the company. The Court ruled that he had committed a breach of trust and was required to account to the company for the value of the shares and the profits realized thereon.

Additional safeguards are provided in the existing legislation pertaining to the issue of the prospectus. It must state who are the directors and proposed directors, the chief executive officers and the auditors of the company; it must give full particulars as to the authorized, issued, and paid up capital, and the different classes of securities

to be issued; it must state the nature of the business to be transacted, and must describe every contract entered into or proposed to be entered into in the name of the company.

If the prospectus contains a false statement every director or proposed director and the promoter or promoters are liable to pay compensation to all persons who subscribe for securities of the company on the faith of the prospectus, for the loss or damage they may have sustained by reason of such untrue statement.

Then, too, a copy of the prospectus signed by every director or proposed director, and dated, must be filed with the Secretary of State. Having filed a copy of the prospectus, the issue of securities must be offered to the public within thirty days, otherwise a new prospectus must be filed. And, if any new contract is entered into other than in the ordinary course of business, no further securities may be offered until a new prospectus describing such contract has been filed with the Secretary of State.

This brief outline of the prospectus provisions is given to show the efforts made by the Legislature to insure that the public may learn as completely as possible the facts about the company whose securities it is asked to purchase. To insure that every applicant may have opportunity to learn these facts, the company is not allowed to accept any application unless the applicant has received a copy of the prospectus at least twenty-four hours before he signs the application.

The Act has recently been amended so that these provisions are made to apply to the underwriter as well as to the company, and it is apparent that the trend in company legislation is to provide for the investing public the maximum safeguard against fraudulent practices in the issue of securities.

A further trend in company legislation is towards the safeguarding of shareholders, bondholders and other present and prospective creditors by requiring that greater publicity be given to the affairs of the company. This is apparent in a recent amendment to the Act by which every public company is required to mail to each shareholder at least fourteen days before its annual meeting a copy of the balance sheet, the statement of income and expenditure and the auditors' report. Any bondholder also is entitled to a copy of such balance sheet, statements and reports. Recent amendments require that much more significant details be given in the published balance sheets and statements of income and expenditure of public companies.

THE DEVELOPMENT OF CAPITALISM FROM 1200 TO 1600

By BENJAMIN HIGGINS

I.—What is "Capitalism"?

FROM a purely economic viewpoint, capitalism means the use of capital in production. A system is "capitalistic" to the degree to which production is roundabout. In this sense, capitalism is as old as mankind. In this sense, too, capitalism exists in all modern societies, regardless of the political system. While this use of the term is most accurate, it is different from popular usage, and is apt to be misleading and inconvenient for historical study.

As used in socialist discussion, "capitalism" stands for all those features of existing economic organization which are obnoxious to the socialists themselves. While Marx does not define "capitalism" formally, it is clear that he regards it as a stage in the historical evolution of society, which is characterized by the concentration of ownership of means of production into the hands of a dominant class, which accordingly exploits labour in order to enhance profits. The existence and intensfication of economic crises is another important feature of the Marxian concept of "capitalism," and monopolization is another. One can show errors in Marx's analysis, but the existence of an entrepreneurial class and of a dependent wage-earning class is one of the features of what is commonly understood as "capitalism," and crises are also.

Sombart considered "capitalism" to be a certain idealized "type" of economic organization, which characterizes a very definite historical period. This "type" of organization developed from 1500 to 1760, was at its height from 1760 until August 1914, and is now on the decline. The capitalistic "type" of economy has certain characteristics. 1. Technical progress is "typical" of capitalism, and in the pre-capitalistic period technique was stable, bound by custom and tradition. 2. Economic freedom—laissez-faire—is also typical of capitalism. Freed from pre-capitalistic control by guilds, municipal authority, manorial customs

and traditions, enterprise was able to make quick use of new improvements, of investment opportunities, etc. 3. Capitalism has its own "spirit," which did not exist previously. It is an unshackled, accumulating, profit-seeking spirit, careless of social consequences and community spirit and the condemnation by church or public. Before capitalism the handicraftsman, and not the capitalist, is the ideal type, bound by allegiance to the Church and the Church opposition to usury, profit-seeking, etc.

While one can point out that Sombart's "capitalism" is in fact typical of no historical period, and that his description of "pre-capitalistic" organization is definitely incompatible with his dates for the beginning of capitalism, nevertheless the existence and adoption of technological improvements are factors which ought to be included in any historical concept of "capitalism." It is also true that the features of "capitalistic" organization can develop more easily where enterprise is relatively free from artificial restraint.

The third of Sombart's "characteristics" was developed by Weber as a cause of capitalism, and will be treated separately as such.

For our purposes it is better not to try to give a formal definition of capitalism, and to be content with an enumeration of its basic elements, which together constitute the economic, socialist and historical concepts of capitalism. These elements are: large-scale commerce, with specialization in commerce; the use of credit, banking operations, a financial class and financial crises; large-scale machine industry; a relatively free entrepreneurial group; agriculture conducted for profit. These are the elements we must look for in a discussion of the development of capitalism.

II.—The "Rise of Capitalism"

Much attention has been directed to the question of the date and causes of the beginning of capitalism. When did it arise, and why?

Karl Marx recognizes the existence of a "sporadic" capitalism in the Mediterranean cities of the 14th and 15th centuries, but dates the "era" of capitalism from the 16th century. He interprets the "rise" of capitalism as a successful struggle of the "capitalist class" against the feudal lords and the guild masters. The basis of its rise was the exploitation of subservient labour. Through the break-up of feudalism and inclosures "a mass of free proletarians was hurled on the labour

market." The old nobility was devoured by wars. Cruel legislation failed to stop the movement. This process of forcible expropriation gained new impetus from the Reformation, and "hurled" the inmates of the monasteries "into the proletariat." The agricultural people were driven from their homes and then maltreated into a condition and discipline suitable for wage labour. The capitalist class rose out of the class of independent farmers who exploited labour, and landlords, and benefited by rising prices. Hand in hand with the break-up of the manor and the expropriation of the peasants went the destruction of domestic industry and the concentration of control of manufacture into the hands of individual capitalists, who gained all the profits. The middle ages contributed two kinds of capital; usurer's capital and merchant's capital. Until the breakdown of feudalism, this capital was prevented from being converted into industrial capital. Exploitation of colonies, slave trade, and monopolies also added to the capital accumulation. [1]

While it is true that capitalism arose as feudalism broke down, Marx does not give a true picture of the process, as will be shown in Section VII. He is also wrong in drawing a sharp line between the late middle ages and the 16th century; the development was gradual.

Sombart was even more emphatic in his distinction between the Middle Ages and the period following the beginning of the 16th century. The mediaeval organization was not only acapitalistic but was one incapable of producing a store of capital. The economy was essentially a localized handicraft one, in which it was difficult enough to obtain a bare subsistence, let alone accumulate capital. Capitalism developed mainly out of the operation of the properties of the feudal lords, and from the increased holdings of urban properties.[2] The fact is that many features of capitalism are to be found in mediaeval economic organization, particularly in commerce, and that commerce was much more important in providing funds for investment than was landholding. Indeed, there is evidence that the commercial capitalists were able to displace the feudal landlords in economic and political control.[3] However, in showing the relation between the rise of the state and of capitalism, Sombart does give a partial explanation. State finance offered one of the best ways for commercial capitalists to enhance their

1. *Marx, "Capital," Chapters XXI to XXXII.*
2. *"Der moderne Kapitalismus," part I.*
3. *Sieveking, V. J. S. W., 1909.*

wealth. (Medici, Fuggers, etc.) It is also true that Church finance has an important influence. The heavy taxes imposed by the popes necessitated the development of both transfer mechanisms and of credit.[1]

The explanation of the "rise of capitalism" which is at once most fascinating and most controversial is Max Weber's. The reason for its development in the 16th century is that the Reformation provided the proper philosophical and ethical setting for the "capitalist spirit" to flourish. Not but that the impulse to acquisition is common to all times and all places; the point is that Roman Catholicism held in check the pursuit of profit and the accumulation of wealth which characterizes capitalism. The problem is not the development of capitalistic activity, but the appearance of the sober bourgeois society in which capitalism reached its apex. Even contemporary society gives us a clue to the rise of this middle class society, for we find that in countries of mixed religion a dominance of Protestants among entrepreneurs, owners of capital, and high grade labour. It was also true that the more highly developed districts were those which gave most support to the Reformation, finding its creed more suitable to aggressive and progressive ways of life. The spirit of capitalism is typified by Benjamin Franklin's "philosophy of avarice." Acquisition of wealth becomes an end in itself. In the middle ages such ideas were considered as the lowest kind of avarice. After the Reformation, such conduct became highly respectable. At the beginning of modern times it was not the existing entrepreneurs who represented the capitalistic spirit, for they were bound by traditionalism; fixed profits, limited interest rates, just wages and just prices. It is in the lower middle class that the spirit was strongest. It was this spirit, and not new streams of money, that stimulated the rise of capitalism. The chief reward for making money was the feeling of having done the job well.

This concept is to be found in Luther's doctrines under the name of the "calling," the idea that each individual is "called" to do a certain job and to do it as well as possible. The highest form of moral conduct is the fulfillment of duty in worldly affairs. The idea of monastic asceticism was extended to worldly life; one should not indulge in luxury. Yet Luther was opposed to monopoly and to usury, and cannot be regarded as the apostle of capitalism. The real enemy of Catholicism

1. Cf. Strieder, J.E.B.H. 1929; Schevill, "Florence"; and esp. Schneider, "Die finanzielien Beziehungen der . . Bankiers . . zus Kirche . ."

was Calvinism. In order to become one of the "chosen," one must work hard and spend little. One must accept one's lot as part of God's scheme. The intensity of worldly activity alone dispels doubts as to being one of the "elect" or not. Pietism was a similar doctrine of predestination which influenced the ascetic movement. Methodism was an Anglo-Saxon movement corresponding to Pietism. In practice, the reasoning of the Baptist sects becomes equivalent to Calvinism.

The net result was to justify the pursuit of wealth, provided that happened to be one's "calling." Poverty was not required, but the pursuit of riches must not lead one to reckless enjoyment. Profits are as holy as wages, and interest is not wrong unless wrung from the poor. The cardinal sin is idleness. As for labourers, only when they were poor did they remain obedient to God; but remaining obedient, they attained eternal happiness in another world. Thus the Reformation gave to the entrepreneur and the capitalist a clear conscience, to pursue profits to the best of their ability. In condemning expenditure, it provided the basis for capital accumulation. The profits of this era were not absorbed into the life of a new nobility, but were reinvested. On the other hand, it justified a marked class distinction, forbade open dissatisfaction on the part of oppressed labour.[1]

This explanation of the rise of capitalism was introduced to English readers by R. H. Tawney, in his "Religion and the Rise of Capitalism." His treatment is essentially the same, but is more general, and develops the thesis in relation to its historical setting. Like Weber, he points out that the Catholic church opposed usury, and emphasized the sin of avarice. The outbursts of commercial activity in the 15th century made the older teaching an economic anachronism. (It will be noted that Tawney is more inclined to say that the Reformation stimulated a movement already under way than was Weber.) The Catholic teaching was an effective barrier to capitalistic development despite its neglect in practice. Tawney attributes less positive influence and more negative influence to Luther than does Weber. Luther, he says, was opposed to the accumulation of wealth, usury, monopoly, high prices, speculation, and the luxury trade with the East. But Calvin's teaching was most characteristic and most influential of the new doctrines. He saw economic life with the eyes of a peasant, and recognized frankly the need for capital, credit and banking, large-scale commerce and finance.

1. "The Protestant Ethic and the Spirit of Capitalism." (English translation, 1926.)

Thrift, diligence, sobriety, frugality, are the Christian virtues, and profits and interest are not necessarily evil gains.

Perhaps the most forceful critic of the theory that the Reformation is responsible for capitalism is H. M. Robertson. He regards his "Aspects of the Rise of Economic Individualism" as a "more realistic treatment," historical rather than sociological. The capitalist, he says, is and always has been a purely secular creature, who sees no reason for religion to meddle in his business affairs. Men do not need to be "called" to the pursuit of riches. Weber's philological interpretation of "calling" is unfounded, and there is no essential difference between Catholics and Puritans on this point. The true interpretation of "calling" savours little of capitalism. Secondly, the "Erwerbsprinzip" is not new; society has been acquisitive for thousands of years. There was plenty of capitalism in the Middle Ages. If we look to Scotland, the birthplace of Calvinism, we find, not an advanced, but a lagging development of capitalism. As for usury, its approval was no part of the Protestant creed; the literature is full of condemnation of it. In practice, Calvin's own attitude towards interest and that of the Catholic church were essentially the same. (One could add here that the Catholic church itself did much to foster capitalism, as shown above.)

Robertson himself emphasizes the rise of the nationalist state, and the Machiavellian philosophy as the bases of capitalism, and in particular the "Price Revolution" following the Discoveries. It is clear that much of Robertson's criticism is justified, but that he goes rather too far in his nihilism with respect to the Reformation. It is fairly generally agreed today that the Protestant ethic was one element in the acceleration of capitalistic development.[1]

Those who associate the "rise of capitalism" with the development of mediaeval commerce tend to stress the Crusades as a series of events leading to rapid progress. These basically religious movements had as their chief results the colonization of unsettled Continental districts, the opening of new Mediterranean markets and ports, the development of the European luxury trade with the Near East, the introduction of

1. The most recent critic of Weber is P. C. G. Walker, in E. H. R. November 1937. He objects to Weber's method of using qualitative rather than quantitative criteria. Moreover, such an investigation cannot take the Reformation as a datum; it must enquire into the causes that lay behind it. He rightly criticizes the emphasis upon the post-16th century history of capitalism. He follows Robertson in emphasizing the price revolution.

new commodities and new techniques into Europe, improved navigation and ships, better organized capital and foreign exchange markets, the beginning of the absorption of the old feudal aristocracy by the new commercial capitalists, the economic development of the Italian cities. Indeed, if one wants to take the risk of picking a single cause for the "rise of capitalism," the Crusades would seem to be it; for out of the commercial capitalism of the Middle Ages and the capital accumulation that it made possible grew the industrial capitalism of later periods.[1] There is danger, of course, that one will fall prey to the "post hoc, ergo propter hoc" fallacy in this connection.

Those who place the period of the "rise of capitalism" at a later date, such as Henri See, usually stress the new geographical discoveries, and the consequent inflow of precious metals, as causes. The most important of these discoveries were the Cape route to the Orient (da Gama, 1498), the North American continent (Columbus, 1492), Brazil (Cabral, 1500), and Magellan's circumnavigation of the globe (1522). Hamilton, while admitting the significance of other factors such as the rise of the national state and improvements in agriculture, regards these discoveries as the great cause of capitalistic development. The effects, according to him, were: 1. Improved shipping. The effect was similar to the effect upon aviation of the trans-Atlantic flights. Bigger and better ships, and new navigation instruments were developed. 2. New techniques; the widening of the market facilitated division of labour and led to technological improvements. 3. The influx of new goods from America and the Orient, including the slave trade. 4. Emigration, which relieved population pressure, provided new raw materials, and markets for finished goods. 5. Guild organization crumbled, unable to deal with new problems, and gave way to the capitalistic employer. 6. The vast influx of gold and silver. This last factor was most important. During the 14th and 15th centuries, expanding output led to declining prices, which acted as a deterrent to expansion. The gold and silver which came first to Spain and Portugal was distributed throughout Europe through the Ricardian specie-flow mechanism. Prices quadrupled, wages and rents lagged, giving an incentive to speculation, capital building, promotion of new industries, etc. Tremendous profits were made from the Oriental trade, and the inflow of gold made possible the importation of Oriental goods. Much of the metal coming from America ended in the Orient.

1. Since the Crusades are mentioned by almost every author who discusses the development of mediaeval commerce and finance, no specific reference is given.

It ought to be pointed out that the mere possession of precious metals cannot provide in and of itself an incentive to capitalism. It is not the general price level, but the relation between the price of consumers' and of capital goods that determines the amount of new investment. It is the profit inflation that is important, due to the lag in costs. Also, the influx of gold made possible the importation of Oriental goods without the necessity of selling an equal value of European goods to the Orient. It thus broadened the area of trade, and provided sources for new profits. Without it, the "unfavourable" trade with the Orient could not have been continued. These points have not been made clear by writers on the subject, including Hamilton himself.

Strictly speaking, one ought not to speak of a "rise of capitalism" as a phenomenon characteristic of any one period or resulting from any one constellation of events. There has been some degree of capitalism in all civilizations, and the features which constitute the present economic organization have been added gradually and one by one. Nor has the trend been one of continual progress. Features of modern capitalism have existed in one period, been abandoned in the next, and then re-introduced, such as investment banking in Venice. One can speak of a "rise of capitalism" only in the sense that the development has been more rapid or more marked in some periods than in others. There is, so to speak, a distinct change in the *third* derivative of the function showing the increased amount of capitalism through time.

III.—Commercial Capitalism

In the period following the Crusades, there existed in Europe a highly organized international trade. The area first to develop was the Mediterranean. While Italian cities took the lead, Spanish cities such as Barcelona and French cities like Marseilles were not far behind. The Mediterranean trade was with North Africa and the Near East, and consisted largely of luxury goods. Ships were quite large, capable of handling good-sized cargoes. The organization was capitalistic, capital being provided mainly through the commenda and societas, and often obtained through issuing shares. Ships were sometimes state owned. Almost contemporaneous with the early development of the Mediterranean trade was the development of the north to south trade. This trade took place through the organization of fairs, such as that of Champagne, or of Antwerp, Lyons, Avignon, Bruges,

Brussels, as well as those of Genoa, Venice, Barcelona, etc. In the conduct of this trade we find considerable division of labour, and the existence of wholesalers, retailers, financiers, etc. The purely northern trade, between Scandinavia and England, England and The Netherlands, Scandinavia and France, etc., was dominated by the Hanseatic League. The important members of the Hanse, like the great Italian traders, were true capitalists earning large profits, and were often able to become nobles on the strength of their financial success. They controlled the peasants and labour, and exerted political influence.

The period following the great discoveries and up to the 18th century is often called the era of "commercial revolution." This term does not give an accurate picture of the period, excluding as it does industrial and agricultural developments, and indicating a change more rapid and more violent than was actually the case. Yet certain trends can be discerned which begin in the late 15th century and continue through the 16th and 17th centuries. First, there was an enormous expansion in European commerce, both domestic and international. France, England and Holland began to rival Italy and Spain as trading countries.

The influence of the discoveries on this expansion can be over-emphasized, and the old trade routes were not abandoned. New ones were added, however, bringing new commodities and new markets. Secondly, there was a relative decline in the importance of the Italian cities and the Hanseatic league in control of international trade. The new routes made the position of the Italian cities less advantageous, while the loss fishing trade and the rise of national states made the Hanseatic league less powerful. Yet the Italian cities continued to dominate the luxury trade until well into the 17th century, and many of the Hanse towns continued to be important economic centres. The commercial revolution finished the overturn of mediaeval organization, with its guilds, its manors, and town control of foreign trade. There was a considerable amount of technical progress in the field of navigation. Ships were built larger and faster, with more decks and more masts, and a combination of square-rigged and lateen sails. Knowledge of currents and winds was enlarged. The science of astronomy made progress, and the compass and astrolobe made possible more efficient navigation on long voyages. Maps and charts were improved, lighthouses built, and harbours cleared. These developments in the field of commerce constitute a part of the development of "capitalism."

IV.—Financial Capitalism

Contrary to Sombart, the development of finance in the Middle Ages had many characteristics that we are inclined to regard as "modern." The most highly developed capital markets were in the Mediterranean cities and in The Netherlands. Commerce was financed to a very large extent by borrowed capital. Capital might be provided under the various "commenda" arrangements, through the "societas," or through the "sea loan." Straightforward loans on personal or commercial security were also made. Often shares were sold to raise capital for ships or cargoes. In Italy and in Spain banks of deposit existed, and payments were made by bank transfers. In certain periods these banks also made loans. Foreign exchange transactions were carried on both as a means of making loans and to transfer capital. The operation of the fairs involved a great deal of sales credit, as did also the transaction of local business. Public finance involved the issue of government securities, state banks, huge international loans, etc. The great financial houses like the Bardi, Peruzzi, Medici, etc., rivalled the Rothschilds and Morgans and Rockefellers of modern times.

The fifteenth and sixteenth centuries, so far as financial capitalism was concerned, were characterized by the spread of these methods of finance to other parts of Europe, notably Germany and England. It might be more accurate to say the development of these financial methods in these countries, since in England at least much use was made of credit in the Middle Ages. In the 16th century, however, England developed its own class of big capitalists, such as Gresham. In Germany, great houses like the Fuggers became internationally significant in the 15th century, and were at their height in the early 16th century. In England the development was continued after the 16th century, her relative importance increasing. During the 16th century Antwerp was the most important international financial centre, overshadowing the Italian cities of Venice and Genoa. The public control of banking made strides in the 15th and 16th centuries. The legal attitude towards credit operations underwent some revision in this period, particularly in England and the northern part of the Continent. Financial capitalism was perhaps more highly developed in Europe up to 1600 than any other form of capitalism.

In this period there occurred the first modern crisis, based not upon famine nor plague nor invasion but upon over-extension of credit. The

break came in 1556, and the panic reached its height in 1559. The depression in the financial market continued for several years afterwards, and the capitalistic development of Europe was retarded as a result. The basis of the credit inflation was Spanish war finance, the Fuggers and other large houses making huge loans to the king. Antwerp was glutted with obligations of the Spanish crown. Gresham noticed signs of disturbance as early as 1553.[1] In France both King and Cardinal were borrowing constantly. In addition to these public loans, an inestimable amount of private credit was extended by merchants, financiers and bankers. In 1557, the war of France and Spain broke out. Philip was advised by the Church to repudiate, but refunded and consolidated for fear of losing his credit altogether. Short time loans were converted into perpetual rentes. Security values fell accordingly. On the date set for payment, only a small part of the interest owed was paid, and the King announced the flotation of a new loan. The market was unable to stand such a strain, and both France and Spain became bankrupt and were forced into peace. The "wars of religion" completed the collapse of the international capital market.[2]

Thus the financial crisis which is a characteristic of the capitalistic system makes its appearance in the 16th century.

V.—Primitive Industrial Capitalism

In a sense, the rise of industrial capitalism can be said to coincide with the decay of feudalism and the rise of the towns. If the rise of towns were a mere transplanting of cottage industry from the manor to a town there would be no basis for such a statement. But in fact the rise of towns involved a change in ownership. The cottage workers no longer owned raw materials and products. The raw materials were supplied either by customers or by merchants who bought the raw materials and sold the finished product for a profit. Such merchants were capitalists, and such artisans were dependent workers, hired for piece-rate wages. Such a change is more significant than the growth of factories as such, for factories existed in ancient times with slave labour. Weber mentions various kinds of factory organizations in the Middle Ages: mills, ovens, breweries, iron foundries. Such organ-

1. *"This Bourse of Antwerp is strange. One day there is plenty of money, and the next none, because there are so many good takers and deliverers that if one will not act, another will. Fugger and Jasper Schetz are bare of money and no good can be done with them at present, as the Emperor owes about 300,000 livres."*
2. *Henri Hauser, J. E. B. H. 1930.*

izations were, however, operated in a communal rather than in a capitalistic manner, with few exceptions. The independent craftsman, the cottage worker, and the putting out system were still predominant. Lipson tells that as late as the 16th century the town craftsmen were forbidden to work at their craft during harvest, in order to be able to work on the manors. It is true that there were large workshops, particularly in the textile industry, during the 16th century. But one must distinguish between increased use of machinery and division of labour on the one hand and a mere collection of workers under one roof on the other. Technical specialization was still relatively rare in the 16th century. Yet mere size does have some significance, and there were some 16th century manufacturers who rose to considerable prominence, and contributed to the accumulation of capital. The trend towards the factory system is discernible in the 16th century, and even in the 15th, as is shown by legislation against large-scale production and the use of machinery. Yet the rise of industrial capitalism is a feature of later centuries.

Technical progress in industry is not a phenomenon which is limited to the period following 1600. One of the earliest and most important advances was the use of water power in place of man or animal power, which opened up many new possibilities in manufacturing. The opposition to its introduction began in the 13th century, and was largely overcome in the early 15th century. The commercial expansion following the discoveries opened up new markets, created new demands, and gave a stimulus to technical progress. Certain new industries grew up: gunpowder mills, cannon foundries, alum and copperas factories, sugar refineries, saltpetre works. Plants were set up involving investments far greater than individual craftsmen or guilds could provide. Even more important than these new industries were the improvements in old industries. Better methods in mining and production of metals were introduced even before the 16th century: drains, pumps, ventilation, etc., in mining; and the blast furnace, water-driven hammers, standardization of metal products, machine-drawn wires, etc., in metallurgy. The substitution of coal for wood and charcoal for heating was important in view of the diminishing lumber supply. The 16th century saw an acceleration of such technological progress. The advantages of calcining iron ore before smelting it was discovered. William Lee invented the stocking frame. The production of salt from sea water

involved large plants. Cranes and pulleys made possible the moving of heavier weights in construction and manufacturing. The finishing of textiles—dyeing, fulling and calendaring—was much improved and done on a large scale. Thus it is clear that so far as technical improvement is concerned the 18th century was more "capitalistic" than the 16th only in the sense that the pace was more rapid and the inventions more striking.[1]

VI.—Enterprise and Control

From the foregoing it ought to be clear that there was a distinct entrepreneurial class in commerce and in finance even in the Middle Ages. During the 16th century, if not earlier, the industrial entrepreneur makes his appearance. To what extent the development of an entrepreneurial class is dependent upon freedom of enterprise is perhaps debatable. Yet there seems to be some support for the contention that the exhausting struggle between the emperor and the pope in the Middle Ages left the cities free to develop under the domination of merchant capitalists. It is at least worth asking, therefore, whether the rise of the national state and the breakdown of town control contributed substantially to the rise of an entrepreneurial class and the growth of capitalism.

That town-and-guild administration involved the setting up of a complicated and lengthy set of rules for trade and commerce there can be no doubt. Severe penalties were imposed for the infraction of rules concerning standards, quality, fraud, adulteration, etc. Particularly important were the laws against forestalling, regrating, and engrossing. An attempt was made to prevent monopolization. The conditions of buying and selling, prices, wages and hours, were determined by law. It would seem that entrepreneurs hemmed in by such restrictions would be discouraged and pine away into insignificance. Yet it is doubtful whether the rules were enforced. It was the impossibility of enforcing the rules against forestalling, etc., that led to price fixing. But while prices were fixed, quantity and quality of commodities varied, so that the *de facto* prices actually fluctuated. The large revenue collected from fines imposed for infringement of rules indicated that the rules were not kept, and that it paid to break them. It is possible, therefore, that town-guild regulation was not such an impediment to capitalistic development as it may appear to be on first sight.

1. Cf. especially J. U. Nef, "The Progress of Technology and the Growth of Large-Scale Industry in Great Britain, 1540-1640," E. H. R. October 1934.

When on the other hand we turn to the state control and mercantilism that succeeded town policy, we do not find much relaxation of the administrative regulation of the economy. Mercantilism involved in practice much more than the control of exports, imports, and the foreign exchanges. As always, it was found that intervention in one part of the economy required intervention in others. Control of foreign exchanges necessitated control of the capital market. Regulation of imports and exports meant the interference with particular businesses. Bullionist policy was extended to emigration and immigration. There were other types of interference not directly related to mercantilism, such as wage regulation, and the legislation against large-scale and machine industry already mentioned.

On the whole, however, it seems probable that the rise of the national state made commerce and industry somewhat more free within and between towns of a particular country, even if town customs taxes and regulations did not immediately appear. Also, if one regards monopoly as typical of capitalism, the mercantilist policy aided the development of capitalism, for the creation of monopolies was a feature of this period. The granting of monopolies to creditors of the State was a mediaeval practice, but the monopolies of the early modern world were more lucrative, and contributed more to the accumulation of capital.

VII.—Capitalistic Agriculture

In so far as the development of capitalism is synonymous with the decay of feudalism,[1] the causes of the break-up of the manor are likewise causes of the rise of capitalism. Since the inclosures did replace serfdom with a free labour class to some extent, and the commutation of labour service for money rents replaced serfdom with more or less free enterprise farming for profit, there can be no doubt that the decay of feudalism was a stimulus to capitalistic development.

The growth of the towns was in part a result of the break-up of the manor, but towns were growing up before the inclosures set in and their growth was also a cause of the decline of feudalism. The existence of an artisan and an entrepreneurial class who did not work land to supply their wants for food, clothing, and raw materials directly meant that markets now existed for exports from the manors located near the towns. Exporting involved specialization of agricultural out-

1. This is the contention of Marx, as we have seen, and Walker's definition (op. cit. p. 10) amounts to the same thing.

put, and specialization is the antithesis of feudalism. The growth of towns stimulated farming for profit rather than farming for consumption.

The growth of towns had another effect through increasing the demand for labour and thus raising wages. This tendency led to the freeing of serfs, and many not freed ran away to take advantage of higher industrial wages.

Another impetus to agricultural specialization was the growth of commerce after the Crusades, and again after the discoveries. These events meant new markets, new commodities, better navigation. The manors could export not only to towns but to other countries. New agricultural methods were introduced into Europe also, which made specialization more profitable.

While there has been some debate on the subject, there can be little doubt that the Black Death accelerated the movement.[1] The immediate effect of the plague and the depopulation resulting from it was an increase in supply of and a decrease of demand for commodities so that prices fell tremendously. Rather than sell livestock and equipment at such prices, landlords sought to acquire more land. This immediate effect was followed by a great reduction in output due to labour scarcity, and prices rose precipitously. This factor made the acquisition of land desirable to expand output and profit by the high prices. But due to the rise in wage rates, it was desirable to find land-intensive rather than labour-intensive industries, such as sheep farming. Here was another reason for enlarging land holdings. The seizure of land was made easier by the frequent arrears in rents due to lack of man-power to obtain the necessary production. The landlords were glad to free villeins because it was too expensive to permit them to go on using the land at the rents fixed in leases in face of the high costs and prices.

There is little evidence of the "struggle" between feudal lord and commercial capitalist that Marx emphasizes, unless the competition for labour can be called a "struggle." Also, it is not true that all the labour freed was forced off the land by the nobility; in many cases the villeins were only too glad to be freed to accept the higher industrial wages. Yet Marx is right in suggesting that feudalism had outlived its usefulness. Indeed, the main reason for its disappearance was its sheer inefficiency and the opportunity for profit in better methods.

1. *Cf. Lipson, "Econ. Hist. of Eng." pp. 82 ff. H. L. Gray in the Eng. Hist. Rev. Oct. 1914; H. Robbins, in J. P. E. Aug. 1928; E. Robo in Eng. Hist. Rev. Oct. 1929.*

Inclosures were accompanied by the concentration of ownership of land into fewer hands. Scattered strips were amalgamated into more workable plots, arable land was converted into pasture, and the commons were appropriated for production. These tendencies were present before the Black Death, but are more noticeable afterwards. Sheep farming was the most important agricultural industry, and yielded large profits.

Thus in the period from the 13th to the 16th centuries, and even afterwards, we notice a gradual transition from farming for consumption to more specialized and more efficient farming for profit, which is one feature of capitalism.

VIII.—Summary and Conclusions

Some elements of capitalism are found in the Middle Ages. Financial and commercial capitalism were particularly well developed, at least in the Mediterranean area. The breakdown of feudalism during the Middle Ages and the accompanying rise of towns introduced new aspects of capitalism. During the 16th century there was considerable development of commercial and financial capitalism in northern Europe. It is questionable whether the rise of the national state was of great significance in this development, but the Crusades, the finance of Church and State, the discoveries and the price revolution, the Reformation, the factors leading to the disappearance of the manor, all played a role. While there was some technical progress and industrialization in this period, industrial capitalism does not typify this era as much as it does the period following 1600.

THROUGH THE WINDOWS OF THE WORLD

ARTHUR G. DORLAND

As we look through the windows of the world today we see a scene of almost indescribable confusion, especially in Central Europe, where the Treaty of Versailles still casts its menacing shadow. But since considerable time must elapse before we see the real significance of the recent Munich Agreement we shall turn our attention to a corner of the world where the rising tide of nationalism released by the Great War is transforming the Near East, and is making the Holy Land, no less than Central Europe, a battle-ground of conflicting national interests.

The Holy Land—"The Too-Much Promised Land"

From earliest times the Holy Land has been a storm-centre of world history. Medieval society was rent asunder for nearly two centuries by the efforts of the Crusaders to recover the holy places from the Moslems. Even as late as the nineteenth century, the quarrels between different religious bodies in Jerusalem set armies marching in Europe and precipitated the Crimean War. Today Jerusalem is still the Holy City of the Christian peoples of the world, the Zion of the Jews, one of the three sacred cities of the Islamic world, and is again a storm-centre where history is in the making.

During the Great War the defeat of the Turkish Empire was hastened by the collapse of its power in Asia Minor as the result of an Arab nationalist revolt led by Emir Feisal. As his father was King of Hejaz and Sherif (or Religious Custodian) of Mecca, the principal Holy City of the Moslem peoples, Feisal was a figure of some importance in Arabia. The famous Colonel T. E. Lawrence was Feisal's right-hand man in this revolt which was an important factor in hastening the conquest of the Holy Land by General Allenby and the ultimate collapse of the Turkish Empire.

The timely assistance of the Arabs had its price, however, *i.e.*, the promise of British recognition of Arabian independence in all Arab territories in Asia Minor, except Aden. This promise was officially given in 1915 by Sir Hugh McMahon, then High Commissioner in Egypt.

Though this pledge was apparently ambiguous in certain of its terms, the Arabs assumed that it applied to Palestine, where they have been for centuries the most numerous inhabitants, as well as to other Arabian territories in Asia Minor. But, though the promise of national independence had inspired the Arabs to assist the allied cause in the Holy Land, their aspirations received rather a serious setback, when about a month before the fall of Jerusalem which concluded Allenby's successful campaign, the famous Balfour Declaration was published announcing the intention of establishing in Palestine a national home for the Jewish people. This was not a new idea, since Zionists attempts had been made during the former Turkish régimé, though with small success. But now with British encouragement and backing, Zionism took a new lease of life as a definitely political and nationalist movement; and the hopes of the whole Jewish world were centered on Palestine, where it was fervently believed a Jewish nation would be reborn and established in a national home. Thus, in a word, the present tangled situation has developed in Palestine because of conflicting promises made by Great Britain to win Arab and Jewish support during the Great War, with the result that the "Too-much Promised Land" has become a battle ground of bitter national rivalries.

In the Peace Settlement after the Great War, the Allies in Council held themselves free to deal with the Arab countries at their discretion, and the earlier promises of Arabian independence were interpreted to suit their own interests. The region which the Arab peoples regarded as Syria was divided into two mandates under the League of Nations, held by Great Britain and France respectively; while several Arabian states were set up to which were arbitrarily assigned frontiers and political régimés most distasteful to the Arabs, and certainly far removed from the national independence which they had been led to expect. The Arab never accepted the post-war carving up of the provinces of the former Turkish Empire, and regards the frontiers that were drawn as illogical and unjust as those that were later wiped off the slate in Central Europe. The case for revisionism in the Near East has been very strong for many years from the Arab point of view, and the end is not yet.

The Clas. Between Arab and Jewish Nationalism in Palestine

Within a few years the same spirit of Arabian nationalism which had inspired their revolt against the Turkish régimé during the Great

War, again swept over the Holy Land and the whole Arabian Peninsula, resulting in the setting up or recognition of Arabian states in Hejez, Yemen, Iraq, Trans-Jordan and Syria. Nor should the movement for Egyptian independence be overlooked in this connection, since it closely parallels the developments in Arabian lands. There are also strong ties of sympathy between the Egyptian and Arabian peoples due to "bonds of fraternity based upon a common language, religion and civilization"—to quote the words of the Egyptian Foreign Minister in a recent speech before the League of Nations Assembly.

This phase of the Nationalist Movement in Arabia first manifested itself in 1920, when Emir Fiesal again led a revolt—this time *against* the British—and thus gained recognition as the king of an independent kingdom of Iraq, entirely free from mandatory control. Some years later the French Mandate over Syria was considerably modified, when in response to the demands of the Syrians for a larger control of their own affairs two semi-independent republics under Moslem presidents were set up by France, with the promise of complete independence within a few years. Thus by 1930 there still remained under direct mandatory control only Palestine, with its eastern section beyond the Jordan River organized as an Arab state *(i.e.,* Trans-Jordan) and controlled by an Arab prince who was well disposed to British rule. But the western section of Palestine, lying between Trans-Jordan and the sea, was claimed by the Zionists as the national home of the Jews in accordance with the promise of the Balfour Declaration. However, the Arabs within this area refuse to recognize the validity of this claim and say that Palestine is an Arab country entitled to self-government and the same degree of independence as was by this time enjoyed by Arabian peoples living in Iraq, Syria, Hejaz and elsewhere.

Under the terms of the Mandate it was understood that to safeguard the interests of the Arab population the number of immigrants entering Palestine was to be determined by reference to the economic capacity of the country to absorb them. In 1918 the Arabs in Palestine numbered about 600,000 to about 55,000 Jews. But the steep rise of Jewish immigration from 9,553 in 1933 to 61,854 within a two-year period suggested the need of immediate action on the part of the Arabs, unless Palestine was to be swamped by Jews and the Arab peoples become a racial minority in a land which had been the Arab national home for centuries. The Zionists, however, looked forward to the time when

they would control the areas on both sides of the Jordan River *(i.e.,* including what is now Trans-Jordan as well as Palestine) making it not only a place of refuge for the Jews but a Jewish state enjoying complete national sovereignty. But the fulfillment of Zionist hopes would mean the reduction of the present Arab majority in Palestine to a minority, facing the possibility of being gradually pushed out of Palestine altogether into the less fertile lands of the interior. As against the possible hardship which this might involve so far as the Arab population of Palestine is concerned, the Zionists place the terrible sufferings of Jewish refugees in Europe and their immediate needs. As a Zionist representative put it in giving evidence before the Royal Commission on Palestine: "When the Arab claim is confronted with our Jewish demand to be saved, it is like the claims of appetite versus the claims of starvation." The Arabs, however, claim that they were not consulted as to whether Palestine should be a place of refuge for the emigrant Jews; and they deny the right of Great Britain or of any power to make Palestine a national home for any other race but their own.

Space does not permit any extended reference to the great economic and material expansion of that part of Palestine under Jewish control. This achievement is based upon three factors principally: (i) increased population *(it is estimated that the Jewish population in Palestine has increased from 55,000 in 1918 to about 410,000 in 1937);* (ii) a Jewish investment of £77,000,000 in the country since 1918; and (iii) the ownership and development of the most fertile areas of Palestine in the Plain of Esdraelon. Agricultural development, which is necessarily slow, has been outstripped, however, by urban growth derived largely from the twofold desire: (i) of providing the largest immediate refuge for European Jews, and (ii) of confronting the Arab population with a compact and defensible Jewish area. Thus Tel Aviv has become the principal Jewish metropolis of the Near East with a population of 150,000 inhabitants, as against 15,000 in 1922; while of Jerusalem's population of 125,000 about 76,000 are Jews. Jews also constitute one-half of the 100,000 inhabitants of Heifa. There is danger, however, that Zionist political enthusiasm may outrun economic realities, and that Palestine may outstrip its rural base. It may well be that the country has already absorbed as many as it can properly support for some years to come, having regard for the natural increase of the Arab and Jewish population now in the country.

A Pan-Arabic and Pan-Islamic Movement in the Near East

The material success of the immigrant Jews in Palestine has greatly benefited the Arab community, and without question the standard of life in this part of Palestine is higher than in other Arab states today. This is, however, a secondary consideration to the Arab in comparison with his national aspirations regarding Palestine, or with his determination to live his own life in his own way. Towards the native Jew in Palestine the Arab has much good will, and they have lived side by side peacefully for centuries. But toward the Jewish immigrants from Central Europe, who are now pouring into the country, the Arab has a very different attitude. Modern Zionism represents to the Arab an alien culture transferred from the West. Against this the Arab places his growing feeling of nationalism which is being fomented by Arab agitators throughout the Near East. In fact, this agitation is rapidly taking the form of a definite Pan-Arabic and Pan-Islamic movement which within the next few decades may assume formidable proportions. For example, a Pan-Arab Congress was held at Bludan—a mountain resort in Syria—in the summer of 1937 which was attended by some 450 delegates from the new Arab states of the Near East, including Egypt, and was definitely called for the purpose of demonstrating Arab solidarity against the partition of Palestine.

The leader of this Nationalist Movement in Palestine is the Grand Mufti or Sherif of Jerusalem, who, as claiming traditional descent from the Caliphs, is religious custodian of the Moslem holy places of Jerusalem. He was also, until deposed by order of the British Government in 1937, president of the Supreme Moslem Council for Palestine. This position gave him control of a very large religious trust fund which he has used effectively for propaganda purposes. Though about one-tenth of the Arab population of Palestine are not Moslems but Christians, these elements have, generally speaking, made common cause with their Moslem compatriots in supporting the idea of Palestine for the Arabs, though they have not been so intransigent in their attitude as the Moslems.

Smouldering Arab opposition to Zionist development of Palestine has flared up recurrently since the first decisive outbreak in 1920, which led to the independence of Iraq. But the Wailing Wall incident in 1929 and the abrupt rise in Jewish immigration to Palestine since 1933 served to bring the situation to a head. The Arabs therefore demanded the

immediate cession of Jewish immigration, and accused the British Government of unduly favouring the Jews, contrary to the terms of the Mandate. At first the Jews themselves were made to feel the Arab resentment of their presence by continued outrages against the property and lives of the Jewish population, which naturally brought reprisals from the Jews. Finally, however, the Arabs directed their efforts not so much against the Jews as against the British régimé in Palestine itself. By 1936 the situation had become so serious that two British divisions were despatched to Palestine to quell the revolt; and a Royal Commission was appointed, with Earl Peel as Chairman, to examine the whole situation and report its findings.

The Palestine Royal Commission Report and Its Failure

The Royal Commission presented its report in June, 1937, and frankly recognizing the incompatible and hopelessly irreconcilable aims of the Arabs and of Zionism, it proposed the partition of Palestine as an alternative policy. The main feature of the proposal was the division of Palestine into three parts, to consist of: (i) a new Jewish state, reduced considerably in area but enjoying independent status; (ii) a new Arab section, comprising the territory to the west of the River Jordan which was to be united to the existing Arab state to the east of the Jordan *(i.e.,* Trans-Jordan); (iii) a small neutral area, including the immediate country around Jerusalem and Bethlehem, with a narrow corridor giving access to the sea at Jaffa, but cutting the proposed Jewish state in two. This area would be a British enclave under mandatory control.

The proposed partition of Palestine in this fashion has been vigorously opposed by both the Zionists and the Arabs. The Jews are bitterly disappointed because the revised boundaries would give them much less than they had hoped to include within their national home, by blocking their expectation of expansion into the regions both east and west of the River Jordan which the Royal Commission has recommended handing over to an enlarged Arab state extending on both sides of the river. Thus in return for the somewhat illusory independent status of the proposed Jewish state, its area would be so reduced as to make it no longer a potential haven for Jewish refugees from Europe in the future as envisaged by the Zionists. The Arabs object that they do not wish to be a racial minority in any state under either Jewish or British control;

while they complain that the Jews have received the most fertile parts of Palestine, the British the most Holy, and the Arabs the most barren.

Altogether the proposed settlement was completely unacceptable to both parties, while it bristled with so many technical and administrative problems that, as Viscount Samuel has aptly observed, "the Royal Commission seems to have picked out the most awkward provisions of the peace treaties of Versailles, and have put a Saar, a Polish Corridor and half a dozen Danzigs and Memels into a country the size of Wales." However, since the Arabs and Jews were unable to produce a constructive plan for peaceful co-operation in Palestine, the British Government, after several years of hesitation, resolutely proceeded to put down all opposition to the partition scheme as outlined by the Royal Commission. For as one Moslem commentator has simply put it: "If two peoples do not desire to live together and neither can put the other out, they must necessarily live apart." Great Britain has therefore continued with the proposed partition, though expressing its willingness to abandon the plan if and when the Arabs and Jews could produce a better one and agree to live and let live. Meanwhile for about three years a bitter civil war has been in progress. A war between what has been called "the government of the day"—*(i.e.,* the British forces and Jewish supernumeraries) and "the government of the night"—*(i.e.,* almost the whole Arab population led by the rebels). Thus a reign of terror now grips this unhappy land reminiscent of the "black and tan" régimé and the gunmen of the Irish Rebellion. Many of the moderate Arabs, taken under the protection of the Government for their own interest, fearing for their lives, have left the country. Arabs carrying passes prescribed by the British Government are liable to be shot by their fellow countrymen as traitors; while those who do not carry passes are liable to arrest or imprisonment by the British military. Hatred and dogged fury, mainly against the British Government, prevail on the Arab side; while the founding of new Jewish settlements every month and the demand for arms for self-protection, based on distrust of British help, express the militant spirit of the young Jewish generation in Palestine today.

A Possible Settlement of the Palestinian Problem

In 1938 the Colonial Secretary, Mr. Malcolm MacDonald, visited Palestine to view conditions for himself; while the Woodhead Commission was appointed to examine the findings of the previous Royal Com-

mission in the light of continued Arab and Jewish opposition to the partition policy. Mr. Winston Churchill, in characteristic vein, vigorously denounced the inability of the British Government to form a coherent opinion on the affairs of Palestine, and charged that all it has been able to do was "to palter, falter, maunder and jibber." Finally the British Government admitted that the partition policy was no longer feasible, and Mr. Malcolm MacDonald proposed calling a conference in London in an attempt to bring together the opposing factions. Accordingly Jews, Arabs and representatives of Arab states contiguous to Palestine are now meeting in London in an attempt to find some mutually acceptable policy which it is hoped will end the present régimé of terrorism and violence in Palestine.

But when Mr. Malcolm MacDonald says with much truth "that peace and prosperity will be restored to Palestine only when the Jews and Arabs realize equally that they must make concessions to each other," there is a third important party to this settlement which will also have to make concessions, namely Great Britain. For as long as all three parties involved in the Palestinian problem are concerned only in the pursuit of their own interests and think of peace only in terms of victory over their opponents, no satisfactory settlement will be possible. Granting, of course, that Great Britain has vital interests in the Near East, it is likely that these interests would be best served, not by the continued frustration of Arabian nationalism by the partition of Palestine, but by the active furthering of the idea of an all-Arabian confederation which might co-operate with or ultimately even include Egypt. Such a federation might consist of three enlarged Arab states: (i) a United Syria *(i.e.,* Trans-Jordan, Syria, Lebanon, Palestine); (ii) Iraq; and (iii) Arabia *(i.e.,* Soudi-Arabia and the Yeman). Such a federation would free the Arab peoples from the post-war divisions of the Western Powers and at the same time recognize the Arab desire for closer association on a truly national basis.

On the other hand, Jewish Zionism must recognize the fact that Palestine is not large enough to meet the major problem of Jewish refugees from Europe today, since there would not be room for all the Jews being persecuted in Central Europe even if there were no Arabs in Palestine. The Holy Land can, nevertheless, make an important contribution to the solution of the Jewish refugee problem, but only a partial one. Great Britain and the Dominions must, therefore, consider

the possibility of Jewish refugees finding homes elsewhere within the Empire, rather than expecting the Arabs to make the major contribution to the solution of this problem. In fact, if other countries would take individually a tenth of the number of Jewish refugees that have gone to Palestine the refugee problem would be settled. We also venture to suggest that Political Zionism confronted with Arabian nationalism of today is no longer a realistic objective, and that without its political aims Zionism could realize many of its material and spiritual ideals in Palestine as a part of a greater Syria under Arab control much better than it could in the old days when under Turkish control. Adequate guarantees would, of course, have to be given for the preservation of the present high standards of social and economic life already achieved by the Jews in Palestine, with perhaps a large measure of autonomy on a cantonal basis. Moreover, the Jews thus situated as a part of a greater Syria, would have a better chance of realizing the spiritual and material ideals of Zionism than if confined within the fixed and narrow boundaries prescribed by partition, the maintenance of which would be a constant source of friction and expense to all parties concerned. Thus with the destructive political and national elements of Zionism relegated to the background, it might attain its principal objectives by peaceful co-operation with the Arabs within an Arab confederation, and so bring order and prosperity to Jews and Arabs alike within Palestine. At the same time the traditional friendship between the Arab peoples and Great Britain, which has been so seriously damaged, would be restored once more to the best interest of all concerned; while those powers at present fighting in the troubled waters of the Near East at the expense of British interests would abandon these tactics as no longer profitable.

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